2230 Michigan Avenue, Suite 200 • Chicago, Illinois 60616 • T 312 881 5856 • F 312 881 5801 • www.cfsinnovation.com

The Center for Financial Services Innovation
An Initiative of ShoreBank Advisory Services

March 24, 2005

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Email: regs.comments@federalreserve.gov

Attention: Docket No. R-1217
Truth in Lending

Dear Ms. Johnson:

I am writing from the Center for Financial Services Innovation (CFSI) in Chicago to comment on the Federal Reserve Board's recent advance notice of proposed rulemaking (ANPR) on open-ended credit, specifically on the regulation of credit cards. CFSI, an initiative of ShoreBank, the largest and oldest community development bank in the country, was formed in early 2004 to help the financial services industry develop innovative products, partnerships and programs that help unbanked families build assets. A crucial aspect of asset-building involves the ability to access and manage a positive credit history. Positive credit is increasingly important in numerous aspects of consumers' lives, as it affects an individual's chances in the job market, in obtaining an apartment, in receiving low-priced car and home insurance, and in purchasing homes and other assets that provide cushions against financial insolvency. While the ANPR addresses a number of issues, CFSI would like to focus on the issues that most affect consumers' ability to build positive credit histories.

Payment Allocation and Late Payments

Evidence shows that credit card companies increasingly consider payments as "late" that were not considered late in the past. A recent survey showed that 58% of banks now have a cutoff time on payment due dates; thus, if the payment is one minute late, consumers are charged a fee. Further, banks have cut grace periods down to 20 days in some cases. If consumers are paying credit card bills in good faith, their credit histories should not be tarnished by late payment policies that are difficult to navigate. The Board should issue a rule requiring creditors to credit payments as of the date they are received, regardless of the time. Moreover, consumers who believe they are paying on time might receive high fee penalties as part of these late payment policies, increasing their revolving credit balances and leading to the possibility that they will be unable to pay the balance in full in the future. Credit card statements might provide "please pay by" dates that do not correspond to grace periods. Companies should provide clear disclosures of due dates and implicate the date at which a payment will be considered late. Financial institutions rely on credit scores and reports to seek out new customers. It is in the best interest of both financial institutions and consumers for customers with positive, on-time payment records to be differentiated from consumers who subject firms to increased risk by not paying bills or by regularly paying late.

Change in Terms and Additional Card Allocation

Some credit card companies have started using “universal default,” a process in which they routinely review a consumer’s credit score and reserve the right to increase his/her rate upon a late payment with any creditor. Thus, if a consumer is late once with Bank X, Bank Y could raise its rate, even in the consumer has never missed a payment with Bank Y. The new rate is often as high as 30% APR. This is particularly problematic given the new late-payment procedures described above. One way to protect consumers against this circumstance would be for the Federal Reserve Board to amend Regulation Z to require 30 days advance notice of a change in rate. Currently, Regulation Z stipulates that advance notice is not required if a rate is increased due to default or delinquency.

Moreover, the Board has asked for comments on whether Regulation Z should be amended to require that additional, unsolicited cards be sent to consumers unactivated. Currently, creditors can send additional activated cards to consumers even when there is no renewal or substitution of a previously issued card. Because all lines of credit affect consumers’ credit scores, consumers should have to opt-in to additional credit lines by activating cards.

Credit Reporting Issues

As previously discussed, credit card companies are increasingly looking into consumers’ credit scores not only at the time of application but throughout the life cycle of card ownership. While companies have been able to levy penalties on consumers for behavior exhibited throughout this life cycle, consumers have not necessarily reaped positive benefits from the other side of the trend. In recent years, the issue of creditors refusing to report positive payments to credit bureaus has arisen, particularly among creditors that offer subprime credit products. This can inhibit a consumer’s ability to build a positive credit history and move into the prime credit market. Credit bureaus have begun to think about ways to incorporate unconventional forms of credit into credit scores, such as FICO’s expansion score product which incorporates payday loans and other nontraditional credit products. Given these industry trends, the Federal Reserve Board should consider ways to ensure that positive as well as negative credit payments are included in consumers’ credit reports, perhaps through best practice guidance.

Thank you for your attention to these comments. Please contact me for further information.

Sincerely,

Jennifer Tescher
Director